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News from State Auditor Crit Luallen's Office

Luallen Releases Audit of Powell County Fiscal Court

(Frankfort December 16, 2008) State Auditor Crit Luallen has released the audit of the financial statements of the Powell County Fiscal Court for the fiscal year ended June 30, 2008. State law requires annual audits of county fiscal courts.

The audit found that the county's financial statements, in all material respects, fairly present the county's assets, liabilities, and equity arising from cash transactions and revenues received and expenditures paid in conformity with the modified cash basis of accounting.

As part of the audit process, the Auditor must comment on non-compliance with laws, regulations, contracts and grants. The Auditor must also comment on material weaknesses involving the internal control over financial operations and reporting.

The audit contains the following comments:

Employees that are part-time should not be permitted to work full-time and be permitted full-time benefits without the approval of the Fiscal Court. During audit testing auditors discovered that employees in the jail and emergency services designated as part-time employees are being permitted to work full-time hours on a regular basis. The County's Personnel Policy and Administrative Code designate a part-time employee as an employee that works less than 35 hours a week on a regular basis. It further says that no employee in the County can be hired without first being approved by the Judge/Executive. Employees that are hired as part-time should not be permitted to work hours that exceed what is permitted by the Personnel Policy. This occurrence has, and will continue to cost the County large sums that were not budgeted for. The audit recommends that the County strictly follow the County's policies and procedures. The audit further recommends the County restrict the hours of part-time employees in order to prevent these employees from receiving benefits that were not approved by the Fiscal Court and Judge/Executive. The Powell County Judge/Executive, Darren Farmer, responded, "We do realize we still need to improve this situation, however we do feel we have

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corrected this somewhat from our last audit comment. We will continue to do our best with this matter.”

The General, Jail, and Disaster Emergency Services Funds have deficits totaling \$931,385. The Powell County Fiscal Court transferred restricted money from the Road, Local Government Economic Assistance (LGEA), Chemical Stockpile Emergency Preparedness Program (CSEPP), and Ambulance Funds to the General, Jail, and Disaster Emergency Services (D.E.S) Funds. The County has repaid a portion of the money; however, additional money was borrowed or transferred during the current fiscal year. A schedule of transfers from restricted accounts and calculation of deficit fund balances is as follows:

<u>Due From</u>	<u>Due To</u>	<u>July 1, 2007</u>	<u>June 30, 2008</u>	<u>Increase/ Decrease</u>
General	Road	\$ 81,558	\$	\$ (81,558)
General	LGEA	10,000		(10,000)
Jail	Road	224,528	253,028	28,500
Jail	LGEA	200,000	200,000	
LGEA	Road		70,000	70,000
DES	Road	1,250	1,250	
DES	CSEPP	3,150	3,150	
DES	Ambulance	700	700	
CSEPP	Ambulance	1,505	1,505	
		<u>\$ 522,691</u>	<u>\$ 529,633</u>	<u>\$ 6,942</u>

	<u>General</u>	<u>Jail</u>	<u>DES</u>	<u>Total</u>
Cash Balance	\$ 19,958	\$ 6,650	\$ 43	\$ 26,651
Interfund Payables		453,028	5,100	458,128
Financing Obligations Payable	500,000			500,000
Fund Balance	<u>\$ (480,042)</u>	<u>\$ (446,378)</u>	<u>\$ (5,057)</u>	<u>\$ (931,477)</u>

KRS 42.455 (2), (3) and (4) specifically prohibits the expenditure of LGEA funds for administration of the government and also states coal impact counties must expend 100% of funds in transportation. The Fiscal Court used a portion of the coal impact funds for expenditures other than transportation. These non-allowable expenditures are due back to the LGEA Fund to be expended for transportation. Also, the Road Fund is restricted for transportation, with the exception of the amount calculated on the Road Fund Allocation Worksheet. The expenditures exceeded the budgeted amount that could be used for purposes other than

transportation during the fiscal year. As a result, the Road Fund is due the amount that was expended in excess of the allowable allocation.

The audit recommends that the Fiscal Court seek guidance from the Department for Local Government and the County Attorney on the necessary actions to be taken to eliminate deficit fund balances. The Powell County Judge/Executive, Darren Farmer, responded, "Funds will be reimbursed as soon as possible."

The County should improve their internal control procedures. The County has a lack of segregation of duties over receipt, disbursement, and record-keeping functions. Typically when one person is in charge of these functions, strong compensating controls are needed. Due to the County's diversity of official operations, small size, and budget restrictions the County has limited options for establishing an adequate segregation of duties. The audit recommends the following procedures be implemented to strengthen internal controls over these various functions:

- An independent person should list all receipts and agree them back to the treasurer's receipts ledger. Also, the employee opening the mail should keep a listing of all checks received for that day, detailing the date received, the check amount, whom it is from, and what the check is for.
- An independent person should open bank statements and review them for unusual items, such as debit memos, and overdraft charges. The person by initialing the bank statement can document this.
- An independent person should review the treasurer's bank reconciliations for accuracy and agree them to book balances for all funds. The person completing this review should initial the bank reconciliation to document that a review was performed.
- An employee independent of check writing and posting duties should match purchase orders to checks and invoices. The employee who signs the checks should cancel the purchase orders and invoices to ensure invoices are not paid twice.
- Access to cash should be limited to cash in regards to occupational tax collections and garbage collections.

The audit recommends the County implement these procedures. This will help segregate the duties of the County employees. The Powell County Judge/Executive, Darren Farmer, responded, "We will implement Internal Control Procedures as much as possible."

The County should improve procedures over expenditures and cash disbursements. During the testing of expenditures, auditors noted that original invoices were not always being maintained. In addition, there were instances where expenditures were being paid from vendor statements rather than an original invoice. Some of the expenditures selected for testing did not have the original supporting documentation or were paid from a vendor billing statement. Auditors also noted that invoices are not being properly cancelled in order to prevent duplicate payment.

The “Uniform System of Accounts” as stipulated by the Department for Local Government requires counties to maintain adequate supporting documentation for all county expenditures. Copies of invoices and faxed invoices are unacceptable. All original invoices should agree to corresponding purchase orders.

The audit recommends the County implement proper accounting procedures and internal control policies. All expenditures should be reviewed and approved by the Fiscal Court prior to payment. Also, disbursements should be made as soon as practical after the Fiscal Court approves the expenditures. Vendors should be paid from original invoices and not the statements mailed periodically from the vendor. All invoices should be cancelled upon payment. Purchasing procedures should be in accordance with Department for Local Government requirements, specifically, purchase orders must include the appropriation account number to which the claim will be posted and proper approval by management or the department head. Vendor names, departments, product descriptions, quantities, and prices should be on each purchase order issued in order for the purchasing procedures to be effective. Sound management and a good internal control structure are essential for the achievement of full oversight and accountability.

Lack of proper accounting practices and internal controls increases the risk that misstatements of financial activity and/or fraud will occur and go undetected by the County. Without proper procedures in place to mitigate the risk, the County is exposing public resources to potential misstatements and/or fraud. The Powell County Judge/Executive, Darren Farmer, responded, “We will watch this more closely on getting original invoices. We will work on our purchase order system.”

The County should include all outstanding debt on the fourth quarter financial statement and improve debt service records. The liability section of the Fourth Quarter Financial Statement submitted to the Department for Local Government and the Debt Disclosure Worksheet received from the County Treasurer were incorrect in regards to principal balances and payments made. Auditors also discovered that there was indebtedness that was not reported on the Fourth Quarter Financial Statement. The audit recommends establishing a liability

register and maintaining it on a current basis. The register would include pertinent data about each open liability, such as date, amount, payee, maturity dates, interest rate, collateral, and payment history with respect to principal and interest. In addition, copies of paid and unpaid liabilities could be included in the register. As a control factor, unpaid principal amounts per the register should be reconciled on a periodic basis to the general ledger. The audit recommends that the County Treasurer maintain accurate records and include all debt and review periodically for correctness. The Powell County Judge/Executive, Darren Farmer, responded, "This was overlooked in our budget process. We will comply with this issue next year. It will also be corrected this year."

The County should prepare an accurate fourth quarter report. The fourth quarter financial report contained posting errors, errors in outstanding checks, ending balances were incorrect and one fund was omitted entirely. The audit recommends the fourth report be completed and reviewed for errors before being submitted to the Department For Local Government. The Powell County Judge/Executive, Darren Farmer, responded, "We will correct future reports. Someone will review reports for errors before submitting to DLG."

The County should approve all interfund transfers. During testing of interfund transfers, auditors discovered that the Treasurer transferred funds prior to receiving Fiscal Court approval. After an extended amount of time, multiple transfers were submitted to the Fiscal Court at the same time for approval.

KRS 68.290 states: "The fiscal court may transfer money from one (1) budget fund to another to provide for emergencies or increases or decreases in county employment pursuant to KRS 64.530 (4). The order of the fiscal court making the transfer shall show the nature of the emergency or personnel increase or decrease and the reason for making the transfer. The fiscal court shall not have any power to transfer money from any sinking fund or special fund raised for a specific purpose until the obligation or purpose for which the fund was raised has been satisfied." The audit recommends the Fiscal Court approve all transfers in the future and provide documentation within the minutes to be in compliance with KRS 68.290. The audit further recommends that the Treasurer seek approval from the Fiscal Court prior to performing interfund transfers. The Powell County Judge/Executive, Darren Farmer, responded, "Treasurer will work on getting approvals by Fiscal Court in the future."

The County should comply with KRS 64.140, which requires that invoices be paid within 30 working days. During the course of the audit, auditors found that numerous invoices were not paid in a timely manner. KRS 65.140(2) states that

all bills for goods or services shall be paid within thirty (30) working days of receipt of vendor's invoice except when payment is delayed because the purchasers has made a written disapproval of improper invoicing by the vendor or by the vendor's subcontractor. It continues to state that if a payment of invoices exceeds 30 days, a 1% interest penalty should be added. The audit recommends that the County comply with KRS 65.140 by paying invoices within thirty (30) working days. The Powell County Judge/Executive, Darren Farmer, responded, "We will correct this as much as possible."

The County should annually review the Administrative Code and make any changes or revisions they deem necessary. KRS 68.005 mentions that the Fiscal Court should review the Administrative Code annually before the end of the fiscal year. The audit recommends that the Fiscal Court review the Administrative Code, Ethics Code and Personnel Policy and then make necessary changes and modifications as appropriate. The review of the Administrative Code should be reflected in the minutes of the Fiscal Court. The Powell County Judge/Executive, Darren Farmer, responded, "This will be corrected. It will be reviewed by Fiscal Court and mentioned in the minutes."

The County should approve a salary schedule. The County did not approve and set the salaries for the County employees. KRS 64.530 states the Fiscal Court of each County shall fix the compensation of every County officer and employee. The audit recommends the County list all employees and each salary or hourly pay rate. The County should also include the starting pay rates for entry-level positions. The County should revise this list as increases are approved by the Fiscal Court. The Powell County Judge/Executive, Darren Farmer, responded, "It will be corrected by Fiscal Court."

This report, in its entirety, can be accessed on the Internet at the following site: www.auditor.ky.gov.